MARATHON OIL COMPANY

IBLA 99-230 Decided May 1, 2001

Appeal from a decision of the Acting Associate Director for Policy and Management Improvement, Minerals Management Service, upholding a value determination regarding the propriety of a processing allowance based on other than actual reasonable processing costs. MMS-96-0386-O&G.

Affirmed.

1. Administrative Appeals–Administrative Authority: Generally--Appeals: Generally--Appeals: Federal Oil and Gas Royalty Simplification and Fairness Act of 1996

   The Federal Oil and Gas Royalty Simplification and Fairness Act of 1996 provides that demands or orders are subject to the 33-month deadline for final decisions of administrative appeals. A "demand" is an order to pay which has a reasonable basis to conclude that the obligation in the amount of the demand is due and owing. An "order to pay" means a written order which (A) asserts a specific, definite, and quantified obligation claimed to be due, and (B) specifically identifies the obligation by lease, production month and monetary amount of such obligation claimed to be due and ordered to be paid, as well as the reason such obligation is claimed to be due, but such term does not include any other communication or action by or on behalf of the Secretary, including value determinations which do not contain mandatory or ordering language.

2. Oil and Gas Leases: Royalties: Natural Gas Liquid Products--Oil and Gas Leases: Royalties: Processing Allowance

   The regulation governing gas processing allowances, 30 C.F.R. § 206.158, states that, where the value of gas is determined pursuant to the provisions of 30 C.F.R. § 206.153, a deduction shall be allowed for the reasonable actual costs of processing. Such costs shall not exceed 66⅔ percent of the value of each gas product determined in accordance with § 206.153, unless a lessee requests, and MMS approves, an allowance that exceeds that percentage. 30 C.F.R. § 206.158(c)(2), (3). To obtain approval to deduct a processing allowance greater than 66⅔ percent, the lessee must demonstrate that the processing costs incurred in excess of the limitation were reasonable, actual, and necessary. 30 C.F.R. § 206.158(c)(3).

3. Oil and Gas Leases: Royalties: Natural Gas Liquid Products--Oil and Gas Leases: Royalties: Processing Allowance

The regulations provide for two methods of determining the gas processing allowance, one involving arm's-length gas processing contracts and the other relating to non-arm's-length gas processing contracts or situations involving no contracts.

4. Oil and Gas Leases: Royalties: Natural Gas Liquid Products--Oil and Gas Leases: Royalties: Processing Allowance

When a lessee has a non-arm's-length processing contract or where there is no contract, including those situations in which the lessee performs processing for itself, 30 C.F.R. § 206.159(b) provides the basis for determining processing allowances. In such cases, the processing allowance will be based upon the lessee's reasonable actual costs. The only way a lessee can obtain relief from the requirement to compute actual costs is to apply for and receive an exception from MMS. 30 C.F.R. § 206.159(b)(4). MMS may grant the exception only if (i) the lessee has arm's-length contracts for processing other gas production at the same processing plant; and (ii) at least 50 percent of the gas processed annually at the plant is processed pursuant to arm's-length processing contracts.

APPEARANCES: Dow L. Campbell, Esq., Findlay, Ohio, for Appellant; Howard W. Chalker, Esq. and Geoffrey Heath, Esq., Office of the Solicitor, U.S. Department of the Interior, Washington, D.C., for the Minerals Management Service.

OPINION BY ADMINISTRATIVE JUDGE PRICE

Marathon Oil Company (Marathon) has appealed an October 22, 1997, decision of the Acting Associate Director for Policy and Management Improvement (Associate Director), Minerals Management Service (MMS), upholding a September 23, 1996, decision on Marathon's request for a value determination issued by the Valuation and Standards Division (VSD) of MMS (Value Determination). 1/ More specifically, on June 10, 1996, pursuant to 30 C.F.R. § 206.153(g), Marathon, as a Federal lessee, requested that its gas processing agreement, 2/ which governed the exercise of its gas processing rights in the Plant, be considered arm's-length under applicable regulations so that it could claim the maximum permitted processing allowance (Request). Marathon's processing costs are based upon the "plant/lease split" 3/ created under the Processing Agreement. (Notice of Appeal and Initial Statement of Reasons for Appeal to the MMS Director filed October 25, 1996, at 1.) In fact, Marathon acknowledged that it was taking, and had been taking, the maximum processing allowance of 66⅔ percent against the value of liquid hydrocarbons extracted from the gas produced from its Federal leases in the Indian Basin Field (Request at 4), which affects valuation for royalty purposes.

1/ On Feb. 1, 1999, Marathon moved to amend its appeal to exclude all time periods prior to Jan. 1, 1996. That motion is granted. On July 13, 1999, Marathon moved to supplement the record with evidence pertaining to the voting structure established by the parties' agreements. That motion is also granted.
2/ Marathon and others executed an Agreement for Construction and Operation of the Indian Basin Gas Plant dated Mar. 30, 1965 (Construction/Operating Agreement). Articles VII and VIII pertain to the execution of a separate processing agreement by which the Plant owners' gas processing rights were to be exercised. Under Article VII, Marathon was authorized to execute processing agreements as Operator of the Indian Basin Gas Plant (Plant). Non-owners could acquire processing rights to the extent capacity remained after Plant owner needs were met, and they also would execute an individual processing agreement.
3/ Under section 9.1.1. of the Processing Agreement, the Plant keeps 75 percent of the value of the liquid hydrocarbons extracted from the gas, while the producer receives the remaining 25 percent, as well as 100 percent of the gas residue as consideration for processing rights. This is referred to as the "plant/lease split." (Request at 3.) As will be more fully discussed infra, a deduction for the reasonable, actual costs of processing is permitted, up to a maximum of 66⅔ percent of the value of each gas product. 30 C.F.R. § 206.158(a), (c)(2). If the 75 percent of value retained by the Plant as consideration for performing processing were accepted as equating to Marathon's actual costs, it would automatically result in the maximum allowance of 66⅔ percent of the value. To exceed that maximum, a lessee must demonstrate that its costs above 66⅔ percent were reasonable, actual, and necessary. 30 C.F.R. § 206.158(c)(3).

Under the Construction/Operating Agreement, Marathon is the Plant Operator, it owns the largest interest in the Plant, and it is a lessee/producer that processes its own gas through the Plant pursuant to its individual Processing Agreement also dated March 30, 1965.

In support of the requested Value Determination, Marathon submitted a copy of the undated proposal to construct the Plant (Proposal), the March 30, 1965, Construction/Operating Agreement, and the Processing Agreement. In addition, Marathon submitted schedules it had prepared showing the history of Marathon's ownership interest in the Plant from 1966 to 1994, gas volumes for March 1995 and February 1996 which were subject to the Processing Agreement, 4/ and an analysis designed to show that the price for processing gas at the Plant is one which an independent party in an arm's-length transaction would be willing to pay. (Request at 3-4.)

Marathon buttressed its position with the March 25, 1996, affidavit of Bob Short, 5/ a chemical engineer who was personally involved in the negotiations that culminated in the Construction/Operating Agreement, and the March 22, 1996, affidavit of Ellis E. Wind, a petroleum engineer who served as Marathon's project engineer for the construction of the Plant, both of which were filed with Marathon's Request. (Exh. D to Request at 1.) These were offered to establish that the United States was fully aware of the planned allocation of the value of the Plant's gas products and "expressed no reservation or objection to such arrangements," thereby suggesting that the Government knowingly consented thereto, and by implication, that it cannot now object to the 66⅔ percent processing allowance that Marathon seeks. (Exh. E to Request at 2.)

Other parties own undivided interests in the Plant which are "equal to the ratio between the productive acreage credited to each party and the total productive acreage credited to all parties in the entire Plant Area.[6/]" (Construction/Operating Agreement, Article IV at 15.) These Plant owners process gas produced from their own leases through the Plant.

4/ Exhibits C, C-1, and C-2 to the Request were prepared to illustrate the percentages of the value of liquid hydrocarbons allocated to all Plant owners and non-owners (Schedule C) in February 1995 and March 1996; gas volumes processed in those 2 months, not including Marathon's volumes (Schedule C-1); and gas volumes in those months supplied by non-owners (Schedule C-2). (Request at 3, n.4.)

5/ Short was employed by Sun Oil Company at the time and has never been employed by Marathon. (Exh. D to Request at 1.)

6/ Every person owning a right to produce gas from within the Plant Area was offered the opportunity to participate in the construction of the Plant and acquire an undivided interest in the Plant area commensurate with the working interest each person owned ("the unsubscribed interest"). If any such person chose not to become a Plant owner, every person who had elected to participate as an owner acquired a portion of the unsubscribed interest in proportion to each participant's percentage of all the interests in the Plant. (Construction/Operating Agreement, Article IV, para. 1 at 13.)

In addition, there are Plant owners who do not process gas through the Plant. When Marathon submitted its Request, it owned a 39.105224 percent interest in the Plant, while non-producers owned approximately 44 percent. 7/ (Request at 2, n.2.) Under the Construction/Operating Agreement, Marathon has the exclusive right to operate the Plant and administer the terms of the Processing Agreement. (Construction/Operating Agreement, Article III at 7; Request at 3.) However, the Operating Agreement also created a voting structure as follows:

> Each party hereto shall have a voting interest on such matters equal to its percentage interest in the Plant as set out on Exhibit "B" as may be revised, hereto attached, and a vote of sixty-five (65%) per cent or more of such voting interest shall be binding upon all of the parties hereto; provided, however, that should any one party at time of voting own sixty-five (65%) per cent or more voting interest, its vote shall not serve to carry or approve such matters unless said vote is supported by one or more of the other parties hereto having a combined interest of at least five (5%) per cent, and provided further that should any one party at the time of voting own more than thirty-five (35%) per cent of the voting interest, its vote shall not serve to defeat or disapprove such matters approved by the vote of parties hereto, unless said party is supported by one or more of the other parties hereto owning a combined interest of five (5%) per cent.

(Construction Operating Agreement, Article III at 11-12.) Before MMS, Marathon argued that "[t]he only reason for a 65% vote was due to the opposing economic interests of the other Plant owners. Otherwise, if all forty owners had the same economic interests, no such vote would have been required. Moreover, Marathon's acquisition of over a 35% interest in the Plant in February 1990 did not permit it to unilaterally veto a 65% vote without the support of a 5% ownership interest." (Request at 3.)

By decision dated September 23, 1996, VSD denied Marathon's Request. In doing so, VSD observed that the Associate Director had previously rejected Marathon's arm's-length argument in Marathon Oil Company, MMS-94-0404-O&G (March 13, 1996), which was then pending before this Board. 8/ In that appeal, which concerned sales of residue gas processed at the Plant between Marathon and U.S. Steel Group, both wholly-owned subsidiaries of USX Corporation, MMS determined that the Indian Basin Processing Agreement involves self-dealing, which rendered the agreement non-arm's length in nature. Noting that nothing had changed with respect to the facts of

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7/ The parties did not provide executed copies of the agreement(s) relating to such non-producer interests.

8/ That appeal, IBLA 96-442, was subject to a global Settlement Agreement and Mutual Release dated Jan. 5, 1999, and was dismissed on motion by order dated Feb. 5, 1999. See also n.1 ante.

Marathon's status as Operator, its ownership of the single largest interest in the Plant, and what MMS characterized in the March 1996 decision as "an effective veto over any decision of the other plant owners," all of which had been considered in that prior decision, VSD adhered to the conclusion that the Processing Agreement was not arm's length. Accordingly, MMS concluded:

> You stated in your letter that Marathon pays royalties on 33-1/3 percent of the value of the gas plant products. As required by the regulations, Marathon must base its non-arm's-length gas processing allowance on the actual, reasonable costs incurred to process the gas, not to exceed 66⅔ percent. You cannot take an automatic 66⅔ percent of the value of the gas plant products as an allowance. We therefore find that Marathon's automatic 66⅔ percent allowance is not proper; Marathon must calculate its non-arm's-length gas processing allowance as required under applicable processing allowance regulations.
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> Based on the above discussion, you must determine value, for royalty purposes, in accordance with the valuation regulations in 30 C.F.R. Part 206 (1996). * * *

(Value Determination at 2.) Marathon timely appealed to the Director of MMS. Finding that Marathon had presented "no arguments in this case that would compel a different result," the Acting Associate Director summarily upheld the September 23rd decision.

[1] Before reaching the substance of Marathon's appeal, we must address a procedural aspect of the case. This Value Determination clearly was appealable under regulations in effect at the time the decision was rendered. 30 C.F.R. § 290.7 (1997). However, the Federal Oil and Gas Royalty Management Act of 1982, 30 U.S.C. § 1724 (1994), as amended by the Federal Oil and Gas Royalty Simplification and Fairness Act of 1996 (RSFA or the Act), 30 U.S.C. § 1724(h) (1998 Supp.), provides that "[d]emands or orders * * * are subject to administrative appeal in accordance with the regulations of the Secretary." 30 U.S.C. § 1724(h)(1) (1998 Supp.). A "demand" is

> (A) an order to pay issued by the Secretary * * * that has a reasonable basis to conclude that the obligation in the amount of the demand is due and owing; or
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> (B) a * * * request by a lessee * * * which asserts an obligation [9/] due the lessee * * * that provides a reasonable

9/ The definition of "obligation" encompasses the principal duty of lessees to either deliver oil or gas in kind or "pay, offset or credit monies," including without limitation, royalties, net profit share, basis to conclude that the obligation in the amount of the demand is due and owing * * * .

30 U.S.C. § 1702 (23) (1998 Supp.).

An "order to pay" means a written order which

(A) asserts a specific, definite, and quantified obligation claimed to be due, and

(B) specifically identifies the obligation by lease, production month and monetary amount of such obligation claimed to be due and ordered to be paid, as well as the reason or reasons such obligation is claimed to be due, but such term does not include any other communication or action by or on behalf of the Secretary * * *. [Emphasis supplied.]

30 U.S.C. § 1702 (26) (1998 Supp.).

The Secretary is required to issue a final decision in an administrative proceeding within 33 months of the date the proceeding was commenced or within 33 months of August 13, 1996, whichever is later. 10/ The failure to issue a final decision within the 33-month period triggers the default provisions set forth in 30 U.S.C. § 1724(h)(2)(A) and (B) (1998 Supp.), and these are defined by reference to the monetary or nonmonetary obligation involved in the proceeding.

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fn. 9 (continued)
proceeds of sale, interest, penalties or assessments on lessees and their designees. 30 U.S.C. § 1702 (25)(B) (1998 Supp.).

10/ The 33-month period may be extended by any time agreed upon in writing by the Secretary and the appellant. Extensions of time had been granted to both parties in this matter, although only extensions requested by an appellant can serve to extend the statutory deadline. Through the mistake and inadvertence of the parties and this Board, the apparent statutory deadline came and went because everyone mistakenly believed that this appeal had been identified in the earlier requests for extensions of time. On Feb. 1, 2000, Marathon and MMS jointly moved this Board to retroactively amend the previous requests for extensions of time to include this appeal. By order dated Feb. 15, 2000, the joint motion was granted. By letter dated Jan. 9, 2001, the parties jointly moved for a further extension through March 1, 2001, which was granted by order dated Jan. 12, 2001. Thereafter, on Mar. 1, 2001, the Board received the parties' third joint motion for a further extension through May 1, 2001. That motion was granted by order dated Mar. 16, 2001.

The parties obviously have understood and treated the September 1996 Value Determination as one subject to RFSA's deadline for final Departmental decisions, and thus they have at least impliedly assumed that it contains the necessary mandatory or ordering language. However, the Value Determination here at issue, even if it could be said to state "a specific, definite, and quantified obligation claimed to be due," clearly does not "specifically identif[y] the obligation by lease, production month and monetary amount of such obligation claimed to be due and ordered to be paid," or "the reason * * * such obligation is claimed to be due." 30 U.S.C. § 1702 (26) (1998 Supp.).

MMS proposed rules to implement the Act in 30 C.F.R. Part 242. Those rules would have explicitly defined the elements that must be contained in an "order." 64 Fed. Reg. 1985 (Jan. 12, 1999). However, MMS instead decided to postpone final action on Part 242, 64 Fed. Reg. 26243 (May 13, 1999). Nevertheless, assuming that this Value Determination properly is subject to RFSA, the parties agreed to extend the statutory deadline, as permitted by 30 U.S.C. § 1724(h)(1) (1998 Supp.). In the future, MMS should simply state whether a Value Determination is subject to the Act, and until rules for Part 242 are finalized, henceforth we will look for the requisite statutory characteristics to eliminate any doubt. 11/

Turning to the substantive issues presented, in its Notice of Appeal and Initial Statement of Reasons (SOR) dated December 2, 1997, Marathon articulates five arguments: the Processing Agreement should be deemed arm's length; it was negotiated at arm's length with the apparent consent of Geological Survey, MMS' predecessor; the split of proceeds between the Plant and the lease is greater than those of the prevailing market; Marathon's ownership interest in the Plant was smaller when the Processing Agreement was executed; and neither Marathon nor any other individual owner possesses veto power over the decisions of other Plant owners. (SOR at 1.) On January 5, 1998, Marathon filed a supplemental SOR, which expanded upon the five arguments noted.

On June 28, 1999, MMS filed its Answer. MMS argues that the Processing Agreement is not an arm's-length agreement, contending that there are no opposing economic interests with respect to that Agreement, and that Marathon and the Plant are affiliated because Marathon controls the Plant. Therefore, MMS argues, the processing allowance must be based upon Marathon's actual reasonable costs and not upon a flat 66⅔ percent deduction. (Answer at 3-7.)

11/ This it must do if future value determinations are to be held subject to RFSA's deadline. In the absence of a definite obligation specifically identified by lease, production month, the amount of the obligation MMS claims is due, the reason it is due (including the test leases and months), and language unambiguously requiring the lessee to report, compute, pay, compute and pay, report production or provide information, it is difficult to apply the default provisions of the Act.

For the reasons which follow, Marathon's contentions are rejected, a conclusion reached by taking a route that is different from the one emphasized by the parties and Judge Irwin. The ultimate question on appeal is whether the Value Determination, which was summarily affirmed by the Associate Director, correctly held that the proper gas processing allowance under Marathon's Processing Agreement is to be computed utilizing actual reasonable costs rather than an automatic 66⅔ percent allowance based upon the 75/25 plant/lease split.

[2] We begin with the regulation governing gas processing allowances. That regulation, 30 C.F.R. § 206.158, states that, where the value of gas is determined pursuant to the provisions of 30 C.F.R. § 206.153, Valuation Standards - processed gas, "a deduction shall be allowed for the reasonable actual costs of processing." Such costs shall not exceed 66⅔ percent of the value of each gas product determined in accordance with § 206.153, unless a lessee requests, and MMS approves, an allowance that exceeds that percentage. 30 C.F.R. § 206.158(c)(2), (3).

To obtain approval to deduct a processing allowance greater than 66⅔ percent, "[t]he lessee must demonstrate that the processing costs incurred in excess of the limitation * * * were reasonable, actual, <u>and</u> <u>necessary</u>." 30 C.F.R. § 206.158(c)(3) (emphasis added). These regulations thus establish the rule that the processing allowance consists of the reasonable, actual costs of processing gas, with a further showing that such costs are necessary when a lessee seeks an exception to exceed the maximum allowance of 66⅔ percent.

[3] As to determining the processing allowance, the regulations provide for two methods, one involving arm's-length gas processing contracts and the other relating to non-arm's-length gas processing contracts or situations involving no contracts. Marathon has expended considerable effort and energy attempting to establish that, under the definition for arm's-length contracts contained in 30 C.F.R. § 206.151, its economic interests are opposed to those of the Plant and that it does not control the Plant. An analysis of the Construction/Operating Agreement and the Processing Agreement leads to a different result.

[4] The regulation governing the determination of processing allowances, 30 C.F.R. § 206.159, contains a section pertaining to arm's-length processing contracts and a separate section addressing non-arm's-length contracts and circumstances involving no contract, including the situation in which the lessee performs processing for itself. The regulation states, in material part, the following:

> (a) *Arm's-length processing contracts*.
> (1)(i) For processing costs incurred by a lessee under an arm's-length contract, the processing allowance shall be the reasonable actual costs incurred by the lessee for processing the gas under the contract, except as provided in paragraphs

> (a)(1)(ii) and (a)(1)(iii) of this section, subject to monitoring, review, audit, and adjustment. The lessee shall have the burden of demonstrating that its contract is arm's-length. * * *
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> (b) *Non-arm's-length or no contract.*
> (1) If a lessee has a non-arm's-length processing contract or has no contract, <u>including those situations where the lessee performs processing for itself, the processing allowance will be based upon the lessee's reasonable actual costs as provided in this paragraph.</u>
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> * * * * * * *
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> (4) A lessee may apply to MMS for an exception from the requirement that it compute actual costs in accordance with paragraphs (b)(1) through (b)(3) of this section. The MMS may grant the exception only if (i) the lessee has arm's-length contracts for processing other gas production at the same processing plant; and (ii) at least 50 percent of the gas processed annually at the plant is processed pursuant to arm's-length processing contracts; * * *. [Emphasis added.]

To apply 30 C.F.R. § 206.159(a), one must resort to the definition of *arm's-length contract*, a term that has been generally defined for use in 30 C.F.R. Subpart D-Federal Gas:

> *Arm's-length contract* means a contract or agreement that has been arrived at in the marketplace between independent, nonaffiliated persons with opposing economic interests regarding that contract. For purposes of this subpart, two persons are affiliated if one person controls, is controlled by, or is under common control with another person. For purposes of this subpart, based on the instruments of ownership of the voting securities of an entity, or based on other forms of ownership:
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> (a) Ownership in excess of 50 percent constitutes control;
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> (b) Ownership of 10 through 50 percent creates a presumption of control; and
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> (c) Ownership of less than 10 percent creates a presumption of noncontrol which MMS may rebut if it demonstrates actual or legal control, including the existence of interlocking directorates.

30 C.F.R. § 206.151, Definitions.

Marathon has argued as if the parties to the Processing Agreement are Marathon and the Plant, a necessary assumption if Marathon is to establish that the Processing Agreement is an arm's-length contract. However, the Plant cannot be a party to the Processing Agreement, because that Agreement expressly identifies the parties and the capacities in which they are executing the contract, and also because the Plant is not a separate entity joint venture and therefore is not a *person,* within the meaning of 30 C.F.R. § 206.151, which defines person as "an individual, firm, corporation, association, partnership, consortium, or joint venture (when established as a separate entity)." The Plant owes its existence to the Construction/Operating Agreement, wherein Marathon and the other Plant owners have defined their relationship:

> It is agreed and understood that by this Agreement and operations hereunder, <u>it is not the intention of the parties hereto to create a partnership or association, or other legal entity</u>. The duties, obligations and liabilities of the parties hereto are intended to be separate and not joint or collective, and nothing contained in this Agreement or in any agreement made pursuant hereto shall ever be construed to create a partnership or association or other legal entity, or to impose any duty, obligation, or liability in any such capacity with respect to any one or more of the parties hereto.
>
> Each party shall be individually responsible for its own obligations as set out in this Agreement and shall be liable only for its proportionate share of the cost and expenses as herein stipulated.
>
> Whenever in this Agreement reference is made to operations for the Plant Account of the parties hereto or to charges or credits to the Plant Account, or whenever similar language is used, the parties use such language merely as a convenient method of referring to the accounting necessary between them, and it is agreed that no such phraseology shall ever be construed as creating any joint liability upon the part of the parties hereto for any obligation incurred under this Agreement, or as setting apart or creating any fund or jointly-owned property for the satisfaction of any such obligation, or as creating a common fund for any other purposes.
>
> Any income from whatever source, due the parties hereto or any of them, and received by Plant Operator hereunder, shall be distributed or accounted for monthly to the party or parties to whom it belongs. [Emphasis added.]

(Construction/Operating Agreement, Article XIV, at 31.)

Consistent with the foregoing expression of intent, the Plant owners established an Accounting Procedure for "joint operations" through which the parties to the Construction/Operating and individual Processing Agreements are billed for their respective shares of cost and expenses. <u>See</u> Exh. "C" to the Construction/Operating Agreement. Therefore, whatever this arrangement is or may be called, it is not, according to the Plant owners, a joint venture which is also a separate entity, 12/ and therefore could not claim to be a *person* on this basis.

If the Plant is not a separate entity joint venture, or a "partnership or association or other legal entity," and its participants have expressly disavowed and contracted against the imposition of "any duty, obligation, or liability in any such capacity with respect to any one or more of the parties" to the Construction/Operating Agreement, it is also not an "individual, firm, corporation, association, partnership, [or] consortium." If we thus accept the plain meaning of the recitals contained in Article XIV, the Plant is not an entity, separate or otherwise, it is merely valuable property which is jointly owned by a number of individuals. 13/ Therefore, this Processing Agreement is an arrangement by and among individuals as the Processor, on the one hand, collectively identified as Marathon Oil Company as Operator and all owners (including Marathon) of interests in the Plant, and Marathon, the Producer, on the other hand: the Plant is not even named as one of the two parties to the March 30, 1965, Processing Agreement here at issue. If the Plant is neither a person nor a party to Marathon's agreement for the processing of its own gas, the arrangement becomes a case of self-dealing or of dealing with an alter-ego, given Marathon's large ownership interest in the joint property (the Plant) and additional role as Operator. Since one cannot contract with oneself as a matter of law, this is a sufficient basis, without more, for finding that there is no contract within the meaning of the gas valuation regulation.

Accordingly, 30 C.F.R. § 206.159(a) is not applicable; 30 C.F.R. § 206.159(b) governs. As set forth above, subsection (b) applies to non-arm's-length contracts and to situations involving no contracts, including where the lessee is processing its own gas. Essentially, the latter is what we have in this case. Marathon executed the Processing Agreement as Plant Operator acting for itself and other Plant owners, and Marathon executed that same agreement as a gas Processor: Marathon is dealing with

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12/ The issue is not whether this is a joint venture, but whether it is a separate entity within the meaning of the gas valuation regulation defining *person*. "A joint venture is frequently defined as an association of two or more persons formed to carry out a single business enterprise * * * for which purpose such persons combine their property, money, effects, skill, and knowledge, without creating a partnership, a corporation, or other business entity." 46 Am Jur 2d § 1, Joint Ventures. J.A. Clawson v. General Insurance Co. of America, 412 P.2d 597, 601 (Idaho 1966); W.B. Johnston Grain Co. v. Self, 344 P.2d 653, 658 (Okla. 1959) ("a joint venture is not a distinct legal entity separate and apart from the parties composing it.")
13/ In fact, under the Joint Accounting Procedure, the Plant is "Joint Property."

itself and processing its own gas. Accordingly, in the circumstances of this case, it is unnecessary to proceed further by analyzing control, but even if it were necessary, we would agree with MMS that Marathon has failed to rebut the presumption of control raised by its 39-percent interest.

Our colleague departs early on in his analysis. He concludes at page 48 of his concurrence that "the joint venture is a 'person' under the definition in 30 C.F.R. § 206.151 with whom Marathon, other producers who are joint venture participants, and others can contract for the processing of gas." He then analyzes whether the Processing Agreement is an arm's-length contract by examining the definition of an arm's-length contract in 30 C.F.R. § 206.151. He first considers whether the parties to the contract have "opposing economic interests." He states at page 49 of his concurrence that "I think it is reasonable to conclude the economic interests of Marathon as a producer and of the joint venture participants are in opposition as to this gas processing agreement." He acknowledges that such a conclusion is contrary to MMS' determination, but he states that he does, "however, agree with its decision that Marathon controlled the plant." Id.

We believe our colleague's conclusion regarding joint ventures is incorrect. The question of including joint ventures in the definition of *person* originally was raised in connection with joint oil field operations for effective reservoir management, to meet spacing requirements, and to share costs in certain Outer Continental Shelf lands and frontier areas, not collaborations to process one's own gas. 52 Fed. Reg. 30775, 30782 (Aug. 17, 1987). Commenters feared that by including *joint venture* in the definition of *person*, the affiliations inherent in joint oil field operations to develop leases would effectively restrict the universe of arm's-length contracts. MMS expressly disavowed any such intention with respect to joint operations of the type identified by the commenters and added the control analysis with its presumptions as a device for allaying those fears. That would be the general case, applicable to most contracts and agreements in the oil and gas industry. MMS obviously viewed situations in which the lessee processes gas differently, and explicitly provided for them in a regulation that applies only to processing agreements.

Moreover, the context of the MMS response on which the Concurring Opinion relies was that of joint ventures "established as separate entities," which, as we have seen, manifestly is not the case at hand. Thus, MMS stated that where the joint venture is established as a separate entity and a party with a controlling interest in that joint venture entity buys production from said entity, the contract is non-arm's-length. To illustrate the opposite case, MMS posited "four totally unaffiliated companies" buying production from the joint venture entity, one of which buys all the production from the other three. MMS concluded that the agreements with the three competitors would be arm's-length, while the purchase from its affiliate, the joint venture entity, would not be arm's-length. 14/

Our colleague next hypothesizes an instance of declining prices which would prompt the producers to curtail processing, on the one hand, while on the other hand, the plant owners' interest would lie in maintaining sufficient processing to keep the plant operating. (Conc. Op. at 49.) While such a hypothesis could, in the proper case, establish the existence of opposing economic interests, no such circumstances are actually presented, suggested or argued in the case at hand, and would not, in any event, change the answer to the question of whether the Processing Agreement constitutes self-dealing with respect to the processing of Marathon's own gas volumes in the Plant.

We do acknowledge, as noted above, that were we to reach the issue of control, we would agree with MMS and our colleague that Marathon controlled the plant. That agreement provides the common ground for our affirmation of MMS' decision in this case.

Accordingly, we find that MMS' Value Determination correctly determined that an automatic 66⅔-percent deduction for processing costs is not the appropriate basis for calculating the allowance, and, absent an exception granted by MMS pursuant to 30 C.F.R. §§ 206.158(c)(3) and 206.159(b)(4), we further find that MMS correctly concluded that Marathon can deduct only its actual reasonable costs for processing its own gas at the Plant.

In light of the disposition of this matter, the requests for a hearing and oral argument are denied.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 C.F.R. § 4.1, the decision appealed from is affirmed. Appellant's request for incorporation is granted; the motion to amend its appeal granted; the request for hearing is denied; and appellant's request for oral argument is denied.

T. Britt Price
Administrative Judge

I concur:

Bruce R. Harris
Deputy Chief Administrative Judge

14/ This latter illustration obviously assumes that the party with a controlling interest in the joint venture entity and the fourth company are affiliated, because the example otherwise makes no sense as an example of a non-arm's-length agreement.

ADMINISTRATIVE JUDGE IRWIN CONCURRING IN THE RESULT:

I. Introduction

Although I agree the gas processing arrangement between Marathon and the Indian Basin Gas Plant cannot be regarded as arm's-length, I reach that conclusion by a different analysis. My own view is that the structure of 30 C.F.R. Part 206 Subpart D, the language of the rules themselves, and MMS' explanation in the preamble to the rules all demonstrate that MMS intended the transportation and processing allowance rules be applied by determining whether there is a contract for these services, and, if so, analyzing whether it is an arm's-length contract. Although I agree that Marathon has not rebutted the presumption that it controls the plant, I do not agree with MMS' conclusion that the agreement "involves self-dealing and is, by its nature, non-arm's-length." If Marathon is self-dealing, then so is every other producer in the field that has its gas processed through the plant and owns a share of the plant.

II. The Regulations in 30 C.F.R. Part 206 Subpart D

It is helpful to begin with an overview of the rules. As is customary, Subpart D begins with definitions that apply "for purposes of this subpart." Two of those definitions, discussed below, are "arm's-length contract" and "person." 30 C.F.R. § 206.151. Standards for valuing unprocessed and processed gas are next (§§ 206.152 and 206.153), followed by rules for determining the quantities and qualities of gas for computing royalties (i.e., the point of royalty settlement, § 206.154) and for accounting for comparison (i.e., so-called dual accounting, § 206.155).

Then come the rules allowing deductions from value for transporting gas (general provisions in § 206.156 and procedures for determining allowances in § 206.157) and for processing gas (§ 206.158, general provisions, and § 206.159, determination procedures). The rules governing determination of allowances, both for transportation and for processing, provide for two methods: a) for arm's-length contracts and b) for non-arm's-length contracts or situations where there is no contract. (§§ 206.157(a), (b); 206.159(a), (b)). Requirements for reporting allowances to MMS also differ between arm's-length contract and non-arm's-length contract or no contract situations. (§§ 206.157(c)(1), (c)(2); 206.159(c)(1), (c)(2)).

It is worth observing that in its subsequent rulemakings governing product valuation MMS has followed this same structure. See Subpart B, Indian Oil, §§ 206.51 (definitions), 206.55(a) (arm's-length contract transportation allowance), 206.55(b) (non-arm's-length or no contract transportation allowance); Subpart C, Federal Oil, §§ 206.101 (definitions), 206.110 (transportation allowance under an arm's-length transportation contract), 206.111 (transportation allowance under a non-arm's-length transportation arrangement); Subpart E, Indian Gas, §§ 206.171 (definitions), 206.178(a) (determining a transportation allowance under an arm's-length contract), 206.178(b) (determining a transportation allowance under a non-arm's-length contract or no contract), 206.180(a) (processing allowance under an arm's-length processing contract), 206.180(b) (processing allowance under a non-arm's-length processing contract or no contract).

When MMS published these rules in proposed form in 1987, it distinguished between arm's-length contract and non-arm's-length contract or no contract situations for both the proposed transportation allowance rule and the proposed processing allowance rule. As to the former, it stated:

> Proposed § 206.157, Determination of transportation allowances, would provide the procedure for determining the transportation allowance. The allowance would be substantially different depending upon whether the lessee has an arm's-length contract with a third party to provide transportation services, or whether the lessee has a non-arm's-length contract or no contract, such as those situations where the lessee has an interest in the pipeline or other transportation system. Paragraph (a) would apply to arm's-length transportation contract situations. * * * Proposed § 206.157(b)(1) provides that if the lessee does not have an arm's-length contract for transporting lease products, but has a non-arm's-length contract or no contract because it has an interest in the pipeline or the transportation facility, then the allowance would be based upon the lessee's reasonable, actual costs of transportation.

52 Fed. Reg. 4732, 4737, 4738 (Feb. 13, 1987). Similarly, MMS stated that proposed 30 C.F.R. § 206.159 "would provide the procedure for determining the processing allowance, which is substantially different depending upon whether the lessee has an arm's-length contract with a plant operator for its processing, or whether the lessee has a non-arm's-length contract or no-contract situation, such as those situations where the lessee has an interest in the gas plant." 52 Fed. Reg. 4732, 4740 (Feb. 13, 1987).

Both as proposed and in the final rule, 30 C.F.R. § 206.159(a) governs processing allowances when there is an arm's-length contract and 30 C.F.R. § 206.159(b) governs "[i]f a lessee has a non-arm's-length processing contract or has no contract, including those situations where the lessee performs processing for itself." That is, § 206.159(b) applies if there is a non-arm's-length contract or if there is no contract, including when the lessee performs processing for itself.

Under the definition in 30 C.F.R. § 206.151, an arm's-length contract is an agreement that "[1] has been arrived at in the marketplace [2] between independent, nonaffiliated persons [3] with opposing economic interests regarding that contract." For purposes of Subpart D, two persons are deemed affiliated "if one person controls, is controlled by, or is under common control with another person" and "[o]wnership of 10 through 50 percent creates a presumption of control * * * based on the instruments of ownership of the voting securities of an entity, or based on other forms of ownership."

A person is defined as any "individual, firm, corporation, association, partnership, consortium, or joint venture (when established as a separate entity)."

When MMS initially proposed the 30 C.F.R. § 206.151 definition of arm's-length contract, it did not refer to free and open markets or adverse economic interests "because the inclusion of such sometimes subjective concepts would make a lessee's determination that its contract was arm's-length subject to uncertainty." 52 Fed. Reg. 4732, 4734 (Feb. 13, 1987). As proposed, the definition read:

> <u>Arm's-length contract</u> means a contract or agreement between independent, nonaffiliated persons. For purposes of this subpart, two persons are affiliated if one person controls, is controlled by, or is under common control with another person, or if one person owns an interest (regardless of how small), either directly or indirectly, in another person.

<u>Id.</u> at 4744. The definition was important, MMS explained, because "MMS is proposing that the gross proceeds under an arm's-length contract would be accepted as value. Other valuation criteria would apply to non-arm's-length contracts." <u>Id.</u> at 4734. "The MMS recognizes that[,] by excluding from the definition those contracts between persons where one party to the contract has any ownership interest in the other, it is narrowing the universe of contracts which would fall within the scope of the definition. * * * The advantage to the proposed definition is that it would be almost purely objective, and lessees and other payors would have assurance that if they pay royalties on the basis of gross proceeds from an arm's-length contract, the royalty valuation would not later be susceptible to redetermination." <u>Id.</u>

The definition of "person," as proposed, was the same as in the final rule, with the exception, as discussed below, that the language "(when established as a separate entity)" was added to the final definition.

The proposed definition of "arm's-length contract" drew many comments. Some Indian and State commenters said the "adverse economic interest and open market" requirements had long been standard criteria for demarcating between arm's-length and non arm's-length contracts. In response, when it adopted the final definition of arm's-length contract, MMS explained:

> The MMS did not adopt the concept of "free and open market" because that concept is highly subjective. However, MMS did include a requirement that the contract be arrived at "in the marketplace" in support of the concept that an arm's-length contract must be between nonaffiliated persons. Also, in furtherance of that concept, MMS included a provision that an arm's-length contract must be between persons with opposing economic interests regarding that contract[,] which means that the parties are acting in their economic self-interest. Thus, although the parties may have common interests elsewhere, their interests must be opposing with respect to the contract in issue.

53 Fed. Reg. 1230, 1239 (Jan. 15, 1988).

Several industry commenters on the proposed definition of arm's-length contract suggested replacing "persons" with "parties." MMS quoted one commenter:

> Involvement in one or more joint operations with a competitor should not be viewed as materially affecting the arm's-length nature of transactions between the firms. However, the reference to "joint venture" in the definition of "person," which is referenced in the proposed definition of arm's-length contract, could be improperly construed as including normal joint field operations conducted under the terms of joint operating or similar agreements. Joint operations clearly involve no interlocking ownership of the instruments of voting securities as between the firms. Joint operations are undertaken to accomplish effective reservoir management, to satisfy spacing requirements, or to share the enormous costs involved in certain OCS and frontier areas.

53 Fed. Reg. 1238 (Jan. 15, 1988).

In response, MMS explained that it did not intend to narrow the definition of arm's-length contract by including joint ventures in the definition of person:

> The definition of "person" includes joint ventures because there are instances where joint ventures are established as separate entities. In those situations, if a party with a controlling interest in the joint venture buys production from the joint venture entity, that contract is non-arm's-length. However, MMS is aware that it also is common for companies to jointly contribute resources to develop a lease and then share the production proportionately. In a situation where four totally unaffiliated companies share the production, if one of the companies buys all of the production from the other three, those three contracts would be considered arm's-length. The company's purchase from its affiliate, of course, would be non-arm's-length.

53 Fed. Reg. 1239 (Jan. 15, 1988).

MMS also dealt with related comments on the proposed definition of "person." Several industry commenters expressed the concern that

> inclusion of joint venture in the definition of person could be extended to oil and gas joint venture operations and further narrow the definition of an arm's-length transaction by clouding the issues of control and affiliation. The sale of hydrocarbons produced through joint venture operations should not be presumed to be other than arm's-length because the individual parties and not the 'joint venture' are responsible for making their own sales of their share of the production.

53 Fed. Reg. 1244 (Jan. 15, 1988). One industry commenter recommended adding the phrase "when established as a separate entity" after the term "joint venture." Id. In accepting this recommendation, MMS commented: "The MMS agrees that two unaffiliated parties jointly developing and producing a lease should not be viewed as one entity unless those parties have formally established a separate entity that involves them both." Id.

III. The Proceedings Before MMS

In MMS-94-0404-O&G, Marathon appealed the June 1994 denial by the Royalty Management Program of its request for an exemption from having to perform an accounting for comparison, under 30 C.F.R. § 206.155, of its sales of gas from the Indian Basin Gas Plant to another wholly-owned subsidiary of USX Corporation. In her March 1996 decision on this appeal, the Associate Director of MMS dealt with the argument by Marathon that the gas processing agreement between it and the Indian Basin Gas Plant should be considered an arm's-length contract. We do not have the record of that appeal before us, so we cannot read what Marathon argued, but the Associate Director's decision states that Marathon argued that because it owned less than 50 percent of the plant, it did not control the plant.

The Associate Director's decision stated:

> Here, the gas processing agreement at issue is between [Marathon] and a gas processing plant in which [Marathon] is the plant operator and holds the single largest share of ownership (38.97 percent). Under Article III of the Agreement for Construction and Operation of the Indian Basin Plant, a vote of 65 percent or more of the voting interest is required for binding approval of an action, thus affording [Marathon] an effective veto over any decision of the other plant owners. [Marathon's] largely unsupported assertion that it and the other plant owners have opposing economic interests is not enough to rebut the presumption of control raised by [Marathon's] percentage [of] ownership and by the other indicia of control enumerated above. Thus, I conclude that [Marathon's] processing agreement involves self-dealing and is, by its nature, non-arm's-length.

March 13, 1996, decision of the Associate Director for Policy and Management Improvement in MMS-94-0404-O&G at 2. The Associate Director affirmed the denial of Marathon's request for an exemption.

In June 1996, Marathon requested approval for calculating its processing allowance under 30 C.F.R. 206.159(a), which governs arm's-length processing contracts. In support of its value determination request, Marathon submitted the Agreement for Construction and Operation of the Indian Basin Gas Plant executed by the parties (referred to collectively as "Processor"); the gas processing agreement between Processor and the producers, signed by a division manager of Marathon as operator of the plant and on behalf of all owners of interests in the plant; and an exhibit showing the volumes of gas produced by Marathon and a dozen other producers that were processed by the plant in 1995.

In her September 1996 letter in response to Marathon's request, the Chief of the MMS Valuation and Standards Division stated that Marathon had raised the same arm's-length issue in its previous appeal; quoted the language from the Associate Director's March 1996 decision set forth above; said no change had occurred either in the agreements or with Marathon's plant ownership percentage; and concluded they were not arm's-length agreements. Therefore, she stated, Marathon must determine value for royalty purposes using the non arm's-length gas processing allowance regulations in 30 C.F.R. § 206.159(b).

On appeal to the Director of MMS, the arguments presented by Marathon and by the Chief of the MMS Royalty Valuation Division in her field report focussed on whether there were opposing economic interests between Marathon and the plant and whether Marathon had rebutted the presumption of control of the plant that is based on the percentage of its ownership of the plant.

"The Agreement," Marathon argued, "is between the Plant, of which Marathon currently owns approximately 39%, and Marathon as a producer in the Indian Basin Field."

> Arguably, under the definition of arm's-length cited above [30 C.F.R. § 206.151], even nonaffiliated parties must prove opposing economic interests. Therefore, we examine the economic interests of a producer of gas versus that of a processor of gas. Where a producer of gas pays a processing fee to a gas plant, the producer's interest is in keeping the fee low, while the processor's interest is in keeping the fee high. These interests are clearly in opposition and thus the Agreement passes the second test of an arm's-length contract.

(Marathon Supplemental Statement of Reasons at 2). Because it owned 39 percent of the plant, there is a presumption of control, Marathon acknowledged. Quoting the language of the Agreement for Construction and Operation that provides that any owner holding more than 35% of the voting interest cannot defeat any matter approved by the other parties unless such an owner garners the support of other owners owning more than a combined interest of 5%, Marathon argued it could not unilaterally veto any decision of the other plant owners. Nor could it bind them without the support of at least 26% of the other owners' interest. Id. at 3-4.

The Chief of the Royalty Valuation Division disputed Marathon's arguments:

> Marathon's arguments are not persuasive and do not rebut the presumption of control * * * . [I]f Marathon's argument were true, no processing agreement would ever be considered non-arm's-length. When a producer is also a processor, the company must rebut the presumption of control and show that it has opposing economic interests. Marathon has not shown that it has opposing economic interests in regard to its processing agreement.

MMS Field Report at 3.

In its response, Marathon argues that the MMS field report statement that "if Marathon's argument were true, no processing agreement would ever be considered non-arm's-length" is misleading: "Marathon has shown that there are opposing economic interests between a producer and a processor[;] however, this test must be coupled with the control test before deciding whether or not an agreement is arm's-length." Marathon Response to Field Report at 2.

Regrettably, the Acting Associate Director's October 22, 1997, decision that is on appeal to us did not discuss these arguments. It merely stated that the issue of whether the gas processing agreement was arm's-length or not had previously been decided and concluded that Marathon had "presented no arguments in this case that would compel a different result" from the March 1996 decision in MMS-94-0404-O&G. Decision in MMS-96-0386-O&G at 2.

IV. The Parties' Arguments On Appeal

On appeal to us the parties argue that whether there is an arm's-length contract involves determining whether there are opposing economic interests between the persons. If there are not, that is the end of the matter. If there are, and one person is presumed to control the other, then the issue is whether that person has carried its burden of rebutting the presumption that they are affiliated.

"The first step under 30 C.F.R. § 206.151 (1996) in determining whether a contract is arm's-length," Marathon argues, "is an analysis of whether the economic interests of the parties are in opposition." Supplemental Statement of Reasons at 2. "Because even non-affiliated parties must pass the opposing economic interests test, this analysis is not concerned with the relationship of the parties, but with the nature of the transaction itself. The opposing economic interests are simply and clearly summarized as: the Plant seeks to maximize processing income, while the producer seeks to minimize processing costs." Id.

"If the parties have opposing economic interests, then the second step in determining whether a contract is arm's-length is a consideration of whether the parties are affiliated. Affiliation is determined by analyzing whether one party controls the other. Although Marathon operates the Plant, it does not 'control' it." Id.

MMS responds that "for a contract to be at arm's-length, the parties must be nonaffiliated and there must be an opposing economic interest regarding the relevant contract. * * * Marathon fails both elements." Answer at 3. MMS argues the gas processing agreement does not involve opposing economic interests between the plant and the owners of the wells who also own the plant: "The well owners constructed the Plant because they believed that was the most profitable alternative to process their gas. * * * [T]he Plant and wells were a combined enterprise to maximize total profit for the combined well and Plant owners." Answer at 3-4.

MMS also argues that Marathon has not met its burden of rebutting the presumption that it controls the plant. "As the operator and greatest single owner, with more than a 35% ownership, [Marathon] could easily obtain the additional 5% vote necessary to defeat matters related to the Plant. Simply put, if Marathon does not control the Plant, no one does." Answer at 6.

In response, Marathon has moved to introduce evidence that "[i]n fact, no one does." Motion to Supplement the Factual Record, filed July 13, 1999.

V. Resolution of the Issues

In my view, the analysis of this case is quite straightforward:

1) Is there a contract for processing the gas?

2) If there is no contract, then the processing allowance is determined under § 206.159(b).

3) If there is a contract, is it arm's-length under the definition in 30 C.F.R. § 206.151?

4) If it is arm's-length, then the processing allowance is determined under § 206.159(a).

5) If it is not arm's-length, then the processing allowance is determined under § 206.159(b).

The gas processing plant in this case is owned and operated pursuant to a joint venture agreement. It is not a joint venture of parties who are developing and producing a lease, as discussed in the preamble to the definitions. Rather, the joint venture participants (referred to in the agreement as "Plant Owners") are the owners of wells or interests in wells in the plant area -- originally forty corporations, partnerships, couples, and individuals -- who entered into the Agreement for Construction and Operation of the Indian Basin Gas Plant in 1965. That agreement is the necessary contractual basis to establish the joint venture, and the plant owners have met the essential requisites of a joint venture: they have contributed money, effort, or skill to the common undertaking; they have a joint property interest in the plant; they have exercised their right of mutual management; and they have an expectation of profit and a right to participate in the profits. See 2 Williston on Contracts (Third Edition, 1959), §§ 318-318A, pages 554, 563-566, § 319; Stott, "Legal and Tax Consequences of Mining Joint Venture Agreements," 18 Rocky Mt. Min. L. Inst. 189, 195-198 (1973).

The language in the agreement -- that the parties do not intend to create a partnership or association or other legal entity and do intend that their obligations and liabilities be separate and not joint -- is standard joint venture agreement language designed to limit tax and other liabilities inherent in other forms of organization. See 4 American Law of Mining (Second Edition), Chapter 121, "Comparative Analysis of Organizational Structures," § 121.05[4]; Chapter 140, "General Negotiating and Drafting Considerations," § 140.03; Chapter 141, "Standard Operating Agreement Provisions," § 141.02; and Title XIII, Joint Exploration and Operating Agreements, Appendix 1, Article IV, Relationship of Participants, § 4.1. Thus, the joint venture is a "person" under the definition in 30 C.F.R. § 206.151 with whom Marathon, other producers who are joint venture participants, and others can contract for the processing of gas. If this joint venture is not a separate entity under that definition, then no joint venture participant who is also a producer of gas can have an arm's-length contract with the joint venture established for processing the gas it produces. Nor, contrary to the statements in the preamble, could any joint venture established for development and production have an arm's-length contract for the purchase of joint venture gas by any joint venture participant.

In this case there is a contract between Marathon and the joint venture, so the question is whether it is arm's-length under the definition in 30 C.F.R. § 206.151.

MMS' responses to the comments on the proposed definition of arm's-length contract indicate that the parties to the processing agreement between the plant and the producers should be regarded as having opposing economic interests if, acting in their economic self-interest, they would under some circumstances have contending views about how or even whether to operate the plant. If, for example, the price of gas or liquids or both were to decline to the point where it would not be profitable for producers to produce gas and pay the costs of its processing, then the producers would seek to curtail processing. The plant owners' interest, on the other hand, would be to maintain sufficient processing to keep the plant operating at the highest possible economic efficiency and to avoid incurring the extraordinary expense of suspending or terminating operations. Such circumstances are certainly foreseeable. See 30 C.F.R. § 206.155(a). I think it is reasonable to conclude the economic interests of Marathon as a producer and of the joint venture participants are in opposition as to this gas processing agreement. Thus, although it does not affect the outcome of this appeal, I do not agree with MMS' decision that Marathon and the joint venture do not have opposing economic interests.

I do, however, agree with its decision that Marathon controlled the plant. I do not find Marathon's argument designed to rebut the presumption that it controls the plant persuasive. That argument is that it has never been able to unilaterally veto any decision of other plant owners because the operating agreement provides the owner of more than 35 percent of the voting interest in the plant must have the support of another 5 percent of the interest owners in order to block an initiative of the remaining owners and that, as the holder of 39 percent of the ownership interest, it needs another 26 percent to commit the plant to any project. Supplemental Statement of Reasons at 3.

Article III of the construction and operating agreement provides that a vote of 65 percent or more of the voting interest is binding on all the parties. It provides further that "should any one party at the time of voting own more than thirty-five (35%) percent of the voting interest, its vote shall not serve to defeat or disapprove such matters approved by the vote of the parties hereto, unless said party is supported by one or more of the other parties hereto owning a combined interest of five (5%) per cent." Marathon's argument that this is not an "effective veto over any decision of the other plant owners" (to use the language of MMS' March 1996 decision) would be stronger if the agreement provided explicitly that under these circumstances a 65 percent vote was not necessary to bind the parties. Even if this is a reasonable interpretation of the agreement, however, what convinces me that Marathon controls the plant is the language of the following paragraph of Article III of the operating agreement, which requires, after the plant is operating, an affirmative vote of 85% or more of the voting interest of the parties for any single expenditure of more than $250,000. Therefore, I do not believe Marathon can be regarded as unaffiliated with the joint venture.

I conclude Marathon has not carried its burden of demonstrating that its gas processing agreement is arm's-length. 30 C.F.R. § 206.159(a)(1)(i). Accordingly, I agree MMS was correct in ordering it to calculate its processing allowance in accordance with 30 C.F.R. § 206.159(b).

I would observe, however, that MMS' October 1997 decision was based on its conclusion that Marathon had presented no arguments that would compel a different result from the March 1996 decision, i.e., on the finding that nothing had changed with respect to the agreements or Marathon's percentage of ownership. It is possible that MMS would come to a different conclusion based on the information Marathon submitted to us in its July 1999 motion to supplement the record, or on more recent information. It is not our province to make that decision in the first instance.

VI. Conclusion

I would add only that I appreciate the parties' agreement, filed in February 2000 -- after the deadline imposed by the Federal Oil and Gas Royalty Simplification and Fairness Act of 1996 for deciding this appeal had expired -- and renewed in January 2001 and again in March 2001, to extend that deadline.

In general, I believe all parties are better served by adopting a reasonable flexibility towards the 33-month period provided in 30 U.S.C. § 1724(h)(1) of that Act -- and, under appropriate circumstances, by awaiting a final Departmental decision on the merits within modest extensions of that period -- than by insisting on a "deemed-decided" decision under the terms of § 1724(h)(2) of the Act. For that reason, in my view it is both permissible and advisable for parties to agree to retroactively extend the deadline, as in this case, just as it is for us to regard an appellant's request for an extension of time to file a pleading as an agreement to extend the deadline even if that agreement does not accompany the request. Irwin, "Appealing Royalty Decisions to the Interior Board of Land Appeals--Putting Your Best Case Forward," Fed. & Indian Oil & Gas Royalty Valuation & Mgmt. III, Paper 5, Pages 5-7 through 5-8 and 5-22 through 5-24 (Order dated March 9, 2000, in Wagner & Brown, IBLA 99-327) (Rocky Mt. Min. L. Fdn. 2000); Fina Oil and Chemical Co., 149 IBLA 168, 186 n. 1 (1999) (appeal filed, Civ. No. 99-2392-HHK (D.D.C.)).

"Had we but world enough, and time," we could request further briefing from the parties, or even grant Marathon's request for oral argument, to help us reconcile our differences in this case.
But we do not.

Will A. Irwin
Administrative Judge